June 2020

Implementation of Tax Reform and AHV Financing in the canton of Lucerne

With the Swiss tax reform, international acceptance of the Swiss corporate tax system is ensured and Switzerland's attractiveness as a business location is maintained. The changes particularly affect the Federal Act on Direct Federal Tax ("DBG") as well as the Tax Harmonisation Act (StHG) and its implementation into cantonal tax law. The reform includes the abolition of the cantonal tax regimes (for holding, mixed and domiciliary companies at cantonal level, as well as for principal companies and the finance branch taxation at Swiss Federal level) and the introduction of internationally recognised replacement measures.

On 19 May 2019, the Swiss electorate passed the tax package with a 66.4 % majority of the votes. No referendum was held against the tax law revision decided by the Lucerne government council. The legislative amendments entered into force on 1 January 2020.

As a result of the abolition of the previous tax privileges, for companies that were previously taxed on a privileged basis ordinary taxation applies as of 1 January 2020, by bringing their tax liability in line with companies subject to ordinary taxation. The canton of Lucerne has already significantly mitigated the implication of TRAF through a 50 % reduction of the ordinary corporate income tax rate back in 2012.

The replacement measures in Lucerne include a patent box with a maximum relief of 10%, adjustments to the capital tax basis, as well as attractive transitional rules for the change of status to ordinary taxation for the period between 2020 and 2024 (or alternatively until 2029).

The replacement measures introduced by the TRAF are being implemented cautiously in the canton of Lucerne. Thanks to its low income tax rate, Lucerne remains within the group of the most attractive business locations in Switzerland.

The following page provides an overview of the most important changes and their effects on corporate taxation in the canton of Lucerne.

If you have any questions, please contact your usual contact at PwC or one of the following experts at PwC Lucerne.

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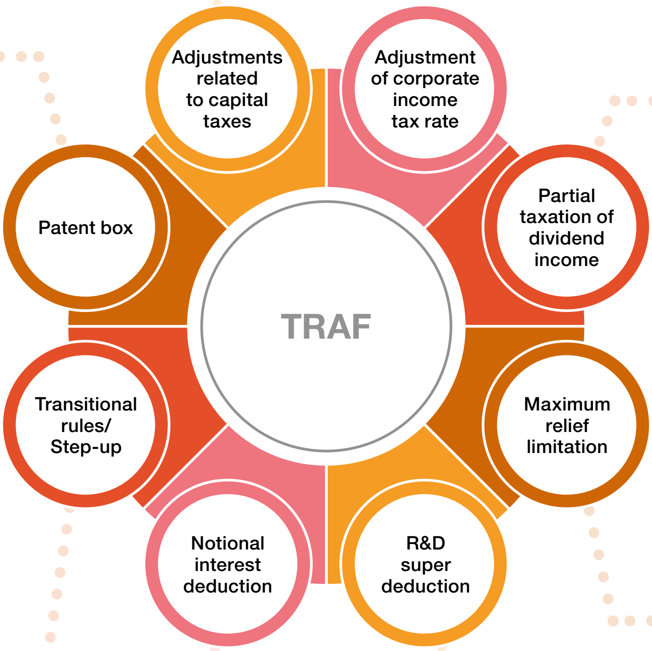
Overview of the most important planned legislative changes with their effects on corporate taxation in Lucerne

Adjustments related to capital taxes
For all legal entities, a uniform capital tax rate of 0.5 ‰ applies (multiplied by tax units of the municipality). Equity attributable to asset categories relating to qualifying participations, patents and group internal financing activities are taxed at a fixed capital tax of 0.01 ‰.

Patent box
The proportion of income from patents and similar rights to the extent it is based on the qualifying research and development expenses (R&D), is included in the calculation of taxable net income with a relief of 10 %. One time entry fee is due upon first time entry into patent box (i.e. taxable add-back to taxable profit) to the extent of the past R&D costs prior to entry into patent box. To the extent of the taxable add-back a taxed hidden reserve has to be made/declared.

Transitional rules / Step-up
The realisation of hidden reserves and self-generated goodwill of companies which were taxed under a privileged regime before will be taxed separately at a rate of 0.4 % (multiplied by tax units of the municipality) for a limited period of 5 years. Alternatively, based on current practice a voluntary disclosure and subsequent depreciation of hidden reserves (current law step-up) for a limited period of up to 10 years remains available until the TRAF enters into force.

Notional interest deduction (NID)
A notional interest deduction on excess equity will **not** be introduced in the canton of Lucerne because of the low ordinary tax rate.



Adjustment of corporate income tax rate
The Cantonal Council of Lucerne rejects the government›s proposed increase in the income tax rate from 1.5 % to 1.6 % per unit. Thus, the effective tax burden (direct federal tax and cantonal tax Lucerne Municipality) remains unchanged at **12.3 %**.

Partial taxation of dividend income
If individuals hold participations of more than 10 % as business assets, the dividends will be considered only partially (i.e. 50 %) for the assessment of the tax base. If individuals hold participations of more than 10 % as private assets, the dividends will be considered only partially (i.e. 60 %) for the assessment of the tax base.

Maximum relief limitation
The cantons are obliged to introduce a limitation for the relief from all TRAF measures combined. In order to remain competitive, the Canton of Lucerne sets in cases of a current law step up the respective limitation at 70 % which is the highest permissible rate. In other words, a quota of only 30 % of the taxable income will remain ordinarily taxed. Where no step-up occurs, maximum relief lies at 20 %.

R&D super deduction
A R&D super deduction will **not** be introduced in the canton of Lucerne.

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